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C O N F I D E N T I A L SECTION 01 OF 03 ANKARA 000253

SIPDIS

EEB FOR ENERGY COORDINATOR MANN
EUR FOR DAS BRYZA

E.O. 12958: DECL: 02/13/2019

TAGS: [ECON](#) [ENRG](#) [EPET](#) [TU](#)

SUBJECT: TURKEY: THE RUSSIAN SIDE OF THE ENERGY EQUATION

REF: A. ANKARA 111

[B](#). 08 ANKARA 2011

[C](#). 08 ANKARA 1688

[D](#). 08 ANKARA 1378

Classified By: Economic Counselor Dale Eppler for reasons 1.4 (B) and (D)

[1](#)1. (C) Summary and comment: Leaving for Moscow on February 12, President Gul said that energy issues will top his agenda in talks with Russian President Medvedev. And for good reason. Russia is Turkey's largest bilateral trading partner, with 70% of Russia's exports consisting of oil and gas. While it is difficult to know exactly what will be discussed in Moscow, there are many likely energy issues for negotiation: the Russian bid on the nuclear power plant, re-negotiation of Turkey's supply contracts with Gazprom, South Stream, Blue Stream II, and Samsun-Ceyhan among others. Taken together, the size and scope for potential cooperation is somewhat alarming given Turkey's current heavy dependence on Russia for energy. Also, we should recognize that Turkey's energy negotiations with Russia cannot be separated from Turkey's other energy negotiations, including with Azerbaijan, because they all affect Turkey's over-arching concern: its future gas supply.

[1](#)2. (C) We rarely draw a link between Turkey's gas contracts with Russia and those with Azerbaijan. However, for the GOT, these are both part of the total supply pool on which it can draw to meet its gas needs. The amount of gas Turkey needs from Azerbaijan is directly related to the amount it will get from other suppliers. With large, important questions of Russian gas supply unresolved and potential domestic gas market liberalization on the table, its understandable why the GOT may not be in a hurry to complete a gas supply contract with Azerbaijan. End summary and comment.

Agenda: What Turkey Wants from Russia

[1](#)3. (C) Renewal of West Line Contract: Turkey's number one energy concern is getting enough gas supply to meet its growing domestic demand for gas. In 2011, a Russian gas contract to supply 6 bcm/a from a pipeline through Bulgaria (named "West Line") will expire. According to Istanbul Total Representative Dilek Altinyay, BOTAS should have opened negotiations to renew this contract long ago, as industry best practices dictate. Why is BOTAS waiting? One possible explanation is that Russia is tying this negotiation to other issues it wants solved (see below). Another explanation is that the GOT plans to use the contract expiration as a way to

bring competition to its domestic gas market by letting private companies make deals directly with Gazprom to import this gas. Energy Ministry Deputy Director General for Energy Issues Nilgun Aciklan told Econoff that the Energy Ministry has drafted a bill to this effect, but Minister Guler has not yet decided whether to submit it to Parliament.

¶4. (C) TPAO's Entry into Russia's Upstream: MFA Energy Department Head Berris Ekinici told us that Gul will support Turkish Petroleum (TPAO)'s request to join Gazprom as an equity partner in developing gas in Siberia. Ekinici declined to mention a specific field, but said it was important for Turkey to be a partner to Russia, not just a consumer of Russian oil and gas.

¶5. (C) Oil for Samsun-Ceyhan Pipeline: Turkey would like to attract Russian and Kazakh oil from the Caspian Pipeline Consortium (CPC) for transport through Turkey to the port of Ceyhan. The GOT has long been interested in creating a "energy hub" in Ceyhan. Such a hub would include refining capacity, storage, expanded export facilities and perhaps an industrial park for petrochemicals and other industries. Russia has not been supportive of Samsun-Ceyhan, however, Russian Deputy Trade Representative in Ankara Rashit Batalov indicated that Russia might be willing to review its position, if Turkey accepted Russia's nuclear bid (see para 9.)

¶6. (C) Approval of Blue Stream II: This is a proposal to build a second pipeline under the Black Sea, parallel to the existing one, to export Russian gas to Turkey. Its not clear

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to what extent Turkey may be pushing this deal. On one hand, it would bring additional gas supplies to Turkey's market. On the other, it increases Turkey's dependence on Russia. Reuters quoted Turkish energy ministry officials as saying that Blue Stream II would be on Gul's agenda in Russia. Acikalin denied this report and Ekinici said the issue was not in Gul's official talking points for the trip. However, she added that if the issue were raised, Turkey is looking at Blue Stream II as part of a North-South corridor, potentially taking gas to Israel, rather than to Europe. She emphasized that Turkey, like the U.S. and Europe, wanted to see the Southern Corridor filled with Azeri, Iraqi and/or Turkmen gas and that diversification from Russian gas remains the primary goal of this corridor.

¶7. (C) However, the PM and FM may have other ideas. According to Ankara-based UK Energy Officer Dan Wilson, PM Erdogan raised the prospect of Blue Stream II as a source for Nabucco in his January discussions with EU Commissioner Barosso. In a January 27 interview with newspaper Radikal, FM Babacan said, "Turkey has invited Russia to join Nabucco. Russia must be involved." Batalov told Econoffs a research institute in Moscow is studying the economics of a gas pipeline twined to the existing line to see whether the best returns come from gas sales to Israel or Europe.

Agenda: What Russia wants from Turkey

¶8. (C) Right to Build Turkey's First Nuclear Power Plant: Batalov told Econoffs that the nuclear bid is the most important agenda item being discussed in Moscow during Gul's visit. He hinted that Russia's award of the nuclear bid could lead to a reconsideration and new openness on other energy deals with Turkey. As examples, he cited the possibility of South Stream not bypassing Turkey and the possibility of oil from the Caspian Pipeline Consortium (CPC) coming to the yet-to-be developed Samsun-Ceyhan oil pipeline, rather than a bypass through Greece.

¶9. (C) The Russian consortium of AtomStroyExport, InterRAO UES and the Turkish firm Park Teknik submitted the only bid in Turkey's tender process to build the first nuclear power

plant. The bid has met all the technical criteria and the only outstanding question is whether the GOT will accept the price per kilowatt hour offered. In January, the Turkish Electricity Trading and Contracting Company (TETAS), the entity conducting the tender, recommended to the Council of Ministers (COM) to reject the bid due to the high price, USD .21 cents/kWh (ref A). The consortium submitted a new price bid and there was some discussion within the GOT whether tender rules allowed for consideration of a second bid. According to local press on February 13, TETAS decided it will evaluate the new bid, with the rationale "it is in the public interest to do so." The new price per kWh quoted was USD .15 cents. According to analysts quoted in the article, if a 3% annual inflation rate is assumed, the net present value of deal is about USD .08-09 cents which is in-line with GOT commitments in other power purchase guarantees. If TETAS recommends the bid be accepted, it will likely receive the rubber stamp of the COM shortly after.

¶10. (C) Approval for South Stream Study: According to the press, and confirmed by Ekinçi, Russia has submitted a proposal to Turkey seeking permission to initiate feasibility studies for South Stream. The planned route for the line would include Turkey's offshore exclusive economic zone, which is why Russia needs Turkey's permission to do a study. This pipeline was designed to bypass Turkey, as well as Ukraine, and take Russian gas to Bulgaria. However, he have heard that there could be something in this deal for Turkey. In separate conversations, both Acikalin and Batalov said there is a nascent proposal for a South Stream spur to Turkey. Neither would give any details.

¶11. (C) Entry into Turkey's Domestic Gas Market: Like SOCAR, Gazprom is interested in Turkey's domestic gas market. Gazprom's Turkish subsidiary, Bosphorus Gas, won a 2005 tender to take over an existing BOTAS-Gazprom contract to import 750 million cubic meters per year. The program called "contract release" was part of a gas market liberalization scheme passed by the Parliament in 2001. However, GOT gas

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price subsidies and licensing issues have kept Bosphorus Gas selling its gas in Turkey (ref B). Energy Minister Guler's advisor Faruk Demir told us that opening and expanding the operations of Bosphorus Gas was a key item of discussion when Gazprom Deputy CEO Medvedev visited Ankara in July 2008.

¶12. (C) In a February 4 visit to Ankara, Lukoil's Chief Executive Vagit Alekperov said that his company plans to spend USD 400 million in Turkey in 2009 in order to double the market share of its local fuel retailer, Akpet, to 10%. Separately, LukOil has agreed with Gazprom on importing and marketing gas to Turkey's domestic market. No further details were given but presumably, this would require Turkey to further liberalize its gas market. Currently, private companies are barred by law from importing gas into Turkey. However, Batalov said Alekperov has over-estimated the importance of the initial agreement LukOil signed with Gazprom. He highly doubted the LukOil would be granted permission to transport gas via Gazprom's network, essentially opening a competition with Gazprom in the markets it already serves, without substantial payments for pipeline upgrades.

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Jeffrey